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C O N F I D E N T I A L SANAA 001103

SIPDIS

NEA/ARP FOR ANDREW MACDONALD
USAID FOR CHRIS KISCO
USTR FOF JASON BUNTIN
DEPT OF COMMERCE FOR TYLER HOFFMAN
DEPT OF TREASURY FOR SAMANTHA VINOGRAD

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TAGS: [ECON](#) [EFIN](#) [EINV](#) [YM](#)

SUBJECT: YEMEN: CONCERN RISES AS FOREIGN EXCHANGE RESERVES
DECLINE

Classified By: Ambassador Stephen A. Seche for reasons 1.4 (b) and (d).

¶1. (U) Summary. As foreign exchange reserves decline, non-ROYG observers have raised a red flag and predicted the impending collapse of the Yemeni rial. The ROYG, however, remains complacent and downplays the threat to the rial's stability. The decline in foreign exchange reserves is reality, and in combination with other economic problems, could very well challenge the ROYG's ability to maintain a stable currency. End Summary.

NON-ROYG OBSERVERS EXPRESS CONCERNS OVER RIAL

¶2. (U) The business community has raised a red flag on the status of Yemen's foreign exchange reserves. General Director of the Federation of Yemen Chambers of Commerce Mohammed A. Al-Maitami, speaking on behalf of members of the private sector, said on May 28 in an open forum that ROYG foreign exchange reserves have dropped by USD 1 billion in the first quarter of this year. (Note: This statement roughly agrees with estimates of the Central Bank of Yemen (CBY), which reported in March that reserves declined from USD 8.1 billion to USD 7.4 billion in 2009. End Note.) Al-Maitami described existing reserves as equivalent to the size of "a postal store in California" and predicted that, in the face of high inflation, the rial would collapse.

¶3. (C) On June 5, political observer and long-time embassy contact Abdulghani al-Eryani outlined a doomsday scenario wherein the ROYG would be unable to either support the rial or pay interest on its treasury bills. He predicted this would cause not only the collapse of the rial, but the banking system as well. He noted that the threat to the rial was not limited to the value of the reserves, but to their liquidity as well. A German diplomat told Pol/Econ Chief this spring that a representative of a large German bank had raised concerns with him about devaluation of the rial, predicting it would lead to significant price inflation.

ROYG COMPLACENT AMIDST FOREIGN RESERVE DECLINE

¶4. (C) Government officials continue to downplay the threat to the foreign exchange reserves. Deputy Finance Minister Jalal Yaqoub told EconOff on June 2 that he was not worried about Yemen's foreign exchange reserves, saying that the ROYG would just print and auction off more local treasury bills to cover any gap. (Comment: This is a stop-gap measure at best. End Comment.) Former Prime Minister Abdul-Karim al-Eryani said that Yemen's foreign exchange reserves are equal to

about six months' imports in a Reuters press report on June 17. He suggested that they are still healthy, but once they reach a level equal to one month's imports, then the ROYG face problems. Salah al-Attar, Director of the ROYG's General Investment Authority (GIA) also dismissed concerns about the declining foreign exchange reserves. He told EconOff on June 1 that the reserves have not been affected by the global financial crisis since the ROYG has instituted a very conservative monetary policy. (Comment: Despite ROYG claims of adherence to conservative investment strategy, official CBY reports have revealed foreign asset losses in the Central Bank as well as in the banking system in general.

End Comment.)

COMMENT

15. (C) While many national economies are suffering from a decline in foreign exchange reserves due to the global financial crisis, the Yemeni economy is particularly at risk as inflation increases, the current account deficit widens, the annual growth rate worsens, and Yemen's main export commodity (oil, at 90 percent of exports) decreases.

Furthermore, the ROYG suffers from a general lack of economic leadership, particularly in managing its budget, which is at least 70 percent dependent upon oil profits, and in removing subsidies on oil, which cost the ROYG USD hundreds of millions per year. The decline of foreign exchange reserves is not an urban legend and combined with other economic problems, it could very well challenge the ROYG's ability to maintain a stable currency. End Comment.

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